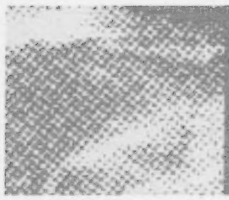
The Manitoba Hydro-Electric Board

Quarterly Report

for the six months ended
September 30, 2017



Report from **The Chair of the Board** and by **The President and Chief Executive Officer**

Financial Overview

Manitoba Hydro's consolidated net loss was $89 million for the first six months of the 2017-18 fiscal year compared to a net loss of $72 million for the same period last year. The increase in the net loss is primarily attributable to restructuring costs driven by the implementation of a significant cost reduction program. Excluding the restructuring expenses, net loss would have been $45 million, an improvement of $24 million over the prior year. The improvement is mostly attributable to favourable water conditions which led to a $32 million improvement in extraprovincial revenues (net of power purchase and water rental expenses) along with $9 million in growth in Manitoba electricity volumes. Higher finance costs and depreciation and amortization expense offset part of these gains. The cost of natural gas is a flow through cost passed onto customers through rates approved by the Public Utilities Board (PUB) and therefore is not a driver for the increase in net loss compared to the prior year.

The consolidated net loss was comprised of a $66 million loss in the electricity segment, a $26 million loss in the natural gas segment, a $2 million net profit in other segments and a $1 million profit impact in adjustments and eliminations.

Manitoba Hydro has seen a significant deterioration in its profit outlook for the 2017-18 fiscal year. The corporation is now forecasting consolidated net income for the year of approximately $40 million. This represents a 44% decrease from 2016-17 net income of $71 million. It also represents almost an 80% drop from our outlook for net income from a reforecast filed with the Public Utilities Board in July. The decrease in forecast is due to the PUB's decision to deny the corporation's request for a 7.9% rate increase as at August 1, 2017, a continuation of weak opportunity export prices, a relatively dry summer impacting water flow conditions and higher financing costs. The forecast assumes average water flow conditions and normal winter weather.

Electric Segment

Revenues from electricity sales within Manitoba totaled $629 million for the six-month period, which was $9 million or 2% higher than the same period last year. The increase in domestic revenue was primarily attributable to an increase in average usage and customer growth, partially offset by weather impacts. Extraprovincial revenues of $275 million were $28 million or 11% higher than the same period last year reflecting higher dependable sales volumes predominantly as a result of higher generation due to favourable water conditions along with modestly higher export prices on opportunity sales. Energy sold in the export market was 6.9 billion kilowatt-hours compared to 6.3 billion kilowatt-hours sold in the same period last year. Other revenues of $15 million were $3 million or 25% higher than the same period last year due to an increase in billable projects for third parties.

Expenses attributable to electricity operations, including the net movement in regulatory deferral balances, totaled $993 million for the six-month period. This represented an increase of $55 million or 6% as compared to the same period last year. The increase was primarily due to a $50 million increase in other expenses, an $8 million increase in net finance expense and a $6 million increase in depreciation and amortization. The increase in other expenses was primarily due to $42 million in restructuring charges associated with the voluntary departure program which launched in April 2017. The increase in net finance expense was primarily the result of foreign exchange losses. The increase in depreciation and amortization was primarily due to new additions to plant being placed into service.

The net loss before net movement in regulatory balances is $113 million. After considering the net movement of $40 million in the regulatory deferral balances, there is a net loss of $73 million of which $66 million is attributable to Manitoba Hydro and $7 million is attributable to non-controlling interest. The non-controlling interest represents Taskinigahp Power Corporation's 33% share of the Wuskwatim Power Limited Partnership's operating results for the first six months of the 2017-18 fiscal year.

Expenditures for capital construction for the six-month period amounted to $1 437 million compared to $1 347 million for the same period last year. Expenditures for the current period included $582 million related to construction of the Keeyask project and $573 million for the Bipole III Reliability Project. The remaining capital expenditures were incurred for ongoing system additions and modifications necessary to meet the electrical service requirements of customers throughout the province. The corporation also incurred $31 million for electric demand side management programs.

Natural Gas Segment

The net loss in the natural gas segment was $26 million for the six-month period compared to a $24 million net loss for the same period last year. The increase in the net loss is primarily due to restructuring costs and warmer weather in the first quarter. Delivered gas volumes were 530 million cubic metres compared to 609 million cubic metres for the same period last year.

Expenses attributable to natural gas operations excluding cost of gas sold amounted to $75 million compared to $73 million for the same period last year.

The net loss before net movement in regulatory balances is $39 million. After considering the net movement of $13 million in the regulatory balances, there is a net loss of $26 million.

Capital expenditures in the natural gas segment were $18 million for the current six-month period compared to $26 million for the same period last year. Capital expenditures are related to system improvements and other expenditures necessary to meet the natural gas service requirements of customers throughout the province. The corporation also incurred $5 million for gas demand side management programs.

Other Segments

The other segments include Manitoba Hydro International Ltd., Manitoba Hydro Utility Services, Minell Pipelines Ltd. and Teshmont Holdings Ltd. The net income was $2 million in other segments for the six-month period compared to net income of $3 million for the same period last year. Revenue was $30 million which was the same as the prior period. Expenses attributable to other segments amounted to $28 million which was $1 million higher than the prior year principally due to foreign exchange losses.

There is also a $1 million profit impact in adjustments and eliminations as a result of the requirement to harmonize accounting policies between electric and natural gas operations related to the gas meter exchange program.

Returning Manitoba Hydro to Financial Health

On July 30, 2017 the PUB awarded Manitoba Hydro a 3.36% interim rate increase, effective August 1, 2017. The corporation's General Rate Application filed with the PUB in May had requested an interim rate increase of 7.9% in August 2017 and a further 7.9% in April 2018.

As a result of the lower interim rate increase, Manitoba Hydro has revised its rate increase targets. The original plan called for a return to financial health over a 10 year period. In addition to accelerated cost reduction goals, the plan envisioned five years of 7.9% rate increases, followed by five years of 2% increases. The revised 10-year plan, inclusive of this year's 3.36% rate award, calls for six years of 7.9% rates increases starting in 2018-19, a 4.54% increase in 2024-25 followed by two years of 2% increases.

The requested rate increases are part of the corporation's plan to restore the utility's financial strength to ensure it can continue to meet Manitobans' energy needs and to keep electric rates lower and more stable for customers in the future. Failing to address Manitoba Hydro's deteriorating financial position in a timely manner substantially increases the likelihood of unexpected and higher rate increases. The 10-year plan includes measures to lower internal operating costs. Already in 2017, Manitoba Hydro has reduced the senior management team by 25% including a 30% reduction to the executive. Since June 1, 325 employees have left the corporation under our Voluntary Departure Program (the VDP) with almost 500 more scheduled to leave by January of 2018. When complete, the VDP will enable close to a 15% reduction in actual staff levels and we anticipate these staff departures will save the corporation over $90 million annually. We are also identifying and aggressively implementing opportunities to manage the business more efficiently and pursuing additional firm sales on the electricity export market.

Without the requested rate increases, the corporation forecasts it will be approximately $800 million short of the cash needed to fund core operations, including investing in the replacement and upgrading of aging infrastructure province-wide, over the next five years. This excludes the cash required to complete the Keeyask Generating Station and Bipole III Reliability Project.

Additional revenue would also help the utility withstand the risks of rising interest rates and drought, and maintain its debt at prudent levels.

A full public hearing before the PUB on Manitoba Hydro's 2017-18 & 2018-19 General Rate Application is scheduled to begin December 4 and end February 9, 2018.

Natural Gas Rate Decrease

In accordance with Manitoba Hydro's methodology to change natural gas rates every quarter depending on the price of gas purchased from Alberta (and as approved by the PUB), rates for residential customers decreased on August 1, 2017 by 4.0% or approximately $29 per year. Rate changes for larger volume customers ranged from decreases of 3.8% to 31.4% depending on the customer class and consumption levels.

The bill impacts are primarily the result of changes in the price that Manitoba Hydro pays for natural gas from Alberta.

Bipole III Reliability Project Approaches Completion

The 1 384-kilometre, high-voltage Bipole III transmission line and the Keewatinohk and Riel converter stations, which link either end of the transmission line, are nearing completion after almost five years of construction.

The transmission line runs from Keewatinohk near Gillam to Riel near Winnipeg and is forecasted to be completed March 31, 2018. The transmission line needs to be ready to use prior to the final in-service date of the stations which is scheduled for July 2018. Two major contractors are working on the transmission line concurrently in northern and southern Manitoba. To maintain completion dates, helicopters are being used for tower installation, hanging of insulators and stringing of conductor wire. Recent milestones include the project reaching two million hours of labour by Indigenous employees and over eight million labour hours in total.

Bipole III will deliver renewable energy to southern Manitoba and will strengthen reliability and security of Manitoba's electricity supply by reducing dependency on the existing HVDC transmission lines and the Dorsey Converter Station.

CNG Filling Station Now in Service

Manitoba Hydro's new compressed natural gas (CNG) station went into service in September. The new station is located on Provincial Road 330 immediately south of the Perimeter Highway in the RM of Macdonald.

The station allows the corporation to provide an alternate supply of natural gas to customers in the event of an outage, such as the fire on TransCanada Corporation's pipeline near Otterburne in January 2014 which left approximately 4 000 homes without natural gas. During the outage, Manitoba Hydro coordinated with TransCanada Corporation and other utilities outside the province to bring CNG in by truck until the pipeline was repaired. However, trucks coming from Saskatchewan were delayed more than three days due to a winter storm. In the interim, many customers purchased electric space heaters to heat their homes. The increased usage put heightened demand on the electrical distribution system.

The CNG station will allow the utility to respond faster to a natural gas outage impacting up to approximately 1 200 customers without threatening the supply of electricity. The station allows two tanker trucks to fill up with CNG and deliver it to local injection points in the natural gas distribution system.

A corporation-owned and maintained CNG station also allows Manitoba Hydro to supply natural gas to customers uninterrupted when conducting repairs and pipeline maintenance on the natural gas distribution system.

H. Sanford Riley
Chair of the Board

Kelvin Shepherd, P. Eng.
President and
Chief Executive Officer
November 14, 2017

Consolidated Statement of Income

In Millions of Dollars (Unaudited)

	Six Months Ended September 30		*Three Months Ended September 30*	
	2017	**2016**	**2017**	**2016**
Revenues				
Domestic – Electric	629	620	308	308
– Gas	88	95	34	36
Extraprovincial	275	247	141	142
Other	43	39	22	18
	1 035	1 001	505	504
Expenses				
Cost of gas sold	53	42	19	19
Operating and administrative	303	302	146	148
Finance expense (net)	324	315	160	156
Depreciation and amortization	210	203	105	102
Water rentals and assessments	64	62	32	31
Fuel and power purchased	57	62	26	31
Capital and other taxes	74	69	37	34
Other expenses	99	47	31	26
	1 184	1 102	556	547
Net loss before net movement in regulatory balances	(149)	(101)	(51)	(43)
Net movement in regulatory balances	53	23	27	17
Net Loss	(96)	(78)	(24)	(26)
Net loss attributable to:				
Manitoba Hydro	(89)	(72)	(20)	(24)
Non-controlling interest	(7)	(6)	(4)	(2)
	(96)	(78)	(24)	(26)

Consolidated Statement of Financial Position

In Millions of Dollars (Unaudited)

	As at September 30	*As at March 31*	*As at September 30*
	2017	**2017**	**2016**
Assets			
Current assets	1 203	1 262	1 587
Property, plant and equipment	21 050	19 757	18 388
Non-current assets	794	753	660
Total assets before regulatory deferral balance	23 047	21 772	20 635
Regulatory deferral balance	608	566	516
	23 655	22 338	21 151
Liabilities and Equity			
Current liabilities	2 023	1 620	954
Long-term debt	16 887	16 102	15 833
Other long-term liabilities	1 554	1 526	1 602
Deferred revenue	724	653	579
Non-controlling interest	184	170	155
Retained earnings	2 810	2 899	2 756
Accumulated other comprehensive loss	(592)	(709)	(786)
Total liabilities and equity before regulatory deferral balance	23 590	22 261	21 093
Regulatory deferral balance	65	77	58
	23 655	22 338	21 151

Consolidated Cash Flow Statement

In Millions of Dollars (Unaudited)

	Six Months Ended September 30		*Three Months Ended September 30*	
	2017	**2016**	**2017**	**2016**
Operating Activities				
Earnings before depreciation, amortization and net finance expense (Adjusted EBITDA)	438	440	241	232
Adjustments for non-cash items included in adjusted EBITDA	(14)	5	(6)	(4)
Adjustments for non-cash working capital accounts	(133)	164	6	239
Net interest paid	(476)	(430)	(235)	(217)
	(185)	179	6	250
Investing Activities	(1 403)	(1 340)	(2 431)	(1 914)
Financing Activities	1 556	1 286	2 190	1 829
Net increase (decrease) in cash	(32)	125	(235)	165
Cash at beginning of period	646	955	849	915
Cash at end of period	614	1 080	614	1 080

Consolidated Statement of Comprehensive Income (Loss)

In Millions of Dollars (Unaudited)

	Six Months Ended September 30		*Three Months Ended September 30*	
	2017	**2016**	**2017**	**2016**
Net Loss attributable to Manitoba Hydro	(89)	(72)	(20)	(24)
Other Comprehensive Income (Loss)				
Items that will be reclassified to income				
Unrealized foreign exchange gains (losses) on debt in cash flow hedges	104	(19)	61	(14)
Items that have been reclassified to income				
Realized foreign exchange (gains) losses on debt in cash flow hedges	13	10	6	5
	117	(9)	67	(9)
Comprehensive Income (Loss) attributable to Manitoba Hydro	28	(81)	47	(33)

Segmented Information

In Millions of Dollars (Unaudited)

	Electric segment		Natural gas segment		All other segments		Eliminations		Total	
Six Months Ended September 30	**2017**	**2016**	**2017**	**2016**	**2017**	**2016**	**2017**	**2016**	**2017**	**2016**
Revenue	920	879	89	96	30	30	(4)	(4)	1 035	1 001
Expenses	1 033	966	128	115	28	27	(5)	(6)	1 184	1 102
Net income (loss) before net movement in regulatory balances	(113)	(87)	(39)	(19)	2	3	1	2	(149)	(101)
Net movement in regulatory balances	40	28	13	(5)	-	-	-	-	53	23
Net Income (Loss)	(73)	(59)	(26)	(24)	2	3	1	2	(96)	(78)
Net income (loss) attribute to:										
Manitoba Hydro	(66)	(53)	(26)	(24)	2	3	1	2	(89)	(72)
Non-controlling interest	(7)	(6)	-	-	-	-	-	-	(7)	(6)
	(73)	(59)	(26)	(24)	2	3	1	2	(96)	(78)
Three Months Ended September 31										
Revenue	458	454	35	37	15	15	(3)	(2)	505	504
Expenses	489	481	56	56	14	13	(3)	(3)	556	547
Net income (loss) before net movement in regulatory balances	(31)	(27)	(21)	(19)	1	2	-	1	(51)	(43)
Net movement in regulatory balances	21	14	6	3	-	-	-	-	27	17
Net Income (Loss)	(10)	(13)	(15)	(16)	1	2	-	1	(24)	(26)
Net income (loss) attribute to:										
Manitoba Hydro	(6)	(11)	(15)	(16)	1	2	-	1	(20)	(24)
Non-controlling interest	(4)	(2)	-	-	-	-	-	-	(4)	(2)
	(10)	(13)	(15)	(16)	1	2	-	1	(24)	(26)
Total assets	23 094	20 620	718	673	90	76	(247)	(218)	23 655	21 151

Generation and Delivery Statistics

	Six Months Ended September 30		*Three Months Ended September 30*	
	2017	**2016**	**2017**	**2016**
Electricity in gigawatt-hours				
Hydraulic generation	17 926	17 291	9 150	8 815
Thermal generation	11	19	9	17
Scheduled energy imports	35	11	12	8
Wind purchases (Manitoba)	428	434	185	185
Total system supply	18 400	17 755	9 356	9 025
Gas in millions of cubic metres				
Gas sales	263	264	89	81
Gas transportation	267	345	124	165
	530	609	213	246

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